



BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

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Application of California-American Water Company (U 210 W), for an Interest Rate of 8.33% for Allowance for Funds Used During Construction (AFUDC) for its San Clemente Dam Memorandum Account and for Authorization to Place the Estimated Annual Average cost of Construction Work in Progress into Rate Base Once the Project is More Certain.

A.07-02-023

**PROTEST
OF THE DIVISION OF RATEPAYER ADVOCATES TO THE
APPLICATION OF CALIFORNIA-AMERICAN WATER COMPANY**

I. INTRODUCTION

Pursuant to Rule 2.6 of the California Public Utilities Commission's ("Commission") Rules of Practice and Procedure ("Rules"), the Division of Ratepayer Advocates ("DRA") files this protest to Application ("A.") 07-02-023. In this application California-American Water Company ("Cal-Am") seeks an interest rate of 8.33% for Allowance for Funds Used During Construction ("AFUDC") for its San Clemente Dam Memorandum Account and it is requesting authorization to place the estimated annual average cost of Construction Work in Progress ("CWIP") into rate base once the project is more certain. The application raises several areas of concern that merit further investigation by the Commission. This Protest provides a non-exhaustive identification of issues that DRA will examine in this proceeding. DRA anticipates that some issues may be resolved, and others may arise, as discovery proceeds. DRA expects that hearings may be necessary to resolve the issues raised by Cal-Am's application.

II. BACKGROUND

Cal-Am is required to upgrade, strengthen, and/or otherwise remedy its aging concrete San Clemente Dam located on the Carmel River in Monterey County in order to

reduce the prospect of its failure as a result of an earthquake or other catastrophic event. The schedule and the nature of the work to be accomplished are unknown at this time; therefore, the Commission in Decision (“D.”) 06-11-050 ordered Cal-Am to remove any existing costs of the retrofit project from its ratebase and establish a memorandum account to track the costs related to this project and to subsequently file this application addressing the ADUFC methodology that should be applied. At some later date, the decision provided that Cal-Am could request recovery of the funds in the memorandum account after Commission review and upon the Commission’s finding that all costs were justified and reasonably incurred.

III. ISSUES

While DRA is still in the process of reviewing Cal-Am’s application, it has identified several issues that it intends to review and address, as necessary, in evidentiary hearings.

A. DRA Opposes Cal-Am’s request for an Interest Rate of 8.33% for AFUDC for its San Clemente Dam Memorandum Account

Cal-Am has proposed to accrue AFUDC at the rate of its fully authorized rate of return (8.33%), which would result in a higher total project cost and higher rates than if AFUDC were to accrue at the current 90-day commercial paper rate. According to Cal-Am’s testimony, besides paying AFUDC expenses, customers will later have to pay the capital cost of the project. (See Exhibit A to A.07-02-023, testimony of David P. Stephenson, Answer 19, at p. 6.)

Instead of accruing AFUDC at the fully authorized rate of return, the 90-day commercial paper rate is the appropriate rate of interest at which Cal-Am’s San Clemente Dam memorandum account should accrue. This is the long-established interest rate authorized for balancing and memorandum accounts that track problematic expenditures including those for long term projects. This rate has been adhered to ever since it was set by the Commission in D.94-06-033 during a rulemaking proceeding that considered the risk of operation of regulated water utilities. Following this policy, the Commission found in D.03-09-022 that the appropriate AFUDC interest for Cal-Am’s proposed

Coastal Water Project was the 90-day commercial rate in lieu of its rate of return because it was uncertain when (or whether) any plant construction would commence, and “[t]herefore, allowing these preliminary costs to earn the utility’s authorized rate of return now carries with it significant risk that the ratepayers may never receive the benefits of these expenditures.” (D.03-09-022, p. 22.) The Commission also adopted this ratemaking treatment (AFUDC at 90-day commercial paper) for the costs of the Carmel River Dam project in D.00-03-053.

According to well-established and sound Commission practice, an investment in plant is only allowed to earn a rate of return once it becomes used and useful. In the case of the San Clemente Dam, it is unclear what alternative will be implemented, when the project will begin, when it will be completed, and whether this dam will ever be used and useful again.

B. DRA opposes Cal-Am’s Request for Authorization to Place the Estimated Annual Average Cost of CWIP into Rate Base Once the Project is More Certain

Cal-Am also proposes to transfer the memorandum account balance into ratebase early-on in the project in spite of the order in D.06-11-050 to remove all project costs from ratebase and place them in a memorandum account for an ultimate review of the reasonableness of the project. The Commission’s anticipated reasonableness review can only take place if Cal-Am follows the Commission’s order by maintaining the memorandum account until the project is complete and all information relating to the accumulated costs is available for a comprehensive review of all related expenditures. As noted above, at this time it is completely unclear when the San Clemente Dam project will even be started, let alone completed. There is still considerable uncertainty as to what will happen with this project or which option will be selected after the environmental impact report is issued. As DRA understands it, Cal-Am’s preferred project alternative is buttressing the dam, yet Cal-Am is also working with other parties to explore the possibility of transferring the San Clemente Dam to a public entity which

would allow the project to then secure public funding for the extra cost associated with the more expensive bypass/removal option preferred by many.¹

This process may take some time. CWIP treatment of water utility construction costs is reserved for projects of short duration, such as those likely to be completed within one year, which is certainly not the case here. (See D.03-09-022, p. 21.) Until the project is fully permitted and work on it complete, costs should continue to be tracked in the previously authorized memorandum account. Once the project is completed, a comprehensive review of costs should be conducted and the project's usefulness evaluated.

Finally, the CWIP issue was litigated in A.05-02-012 and decided in D.06-11-050 and it should not be relitigated here. At a minimum, the principles of *res judicata* suggest that Cal-Am should accept the Commission's earlier determinations regarding this issue.

IV. CATEGORIZATION AND PROPOSED SCHEDULE

DRA agrees with Cal-Am's proposed categorization of this proceeding as rate setting. Evidentiary hearings may be necessary to resolve the issues raised in Cal-Am's application. Therefore, DRA requests that a prehearing conference be held to establish a schedule for this proceeding.

Cal-Am's application raises complex issues. Furthermore, the proceeding will have significant financial and policy implications. DRA anticipates that this proceeding will require a considerable amount of research and discovery. In order to perform the research and discovery necessary to evaluate the issues raised by Cal-Am's application thoroughly, DRA will require substantially more time than suggested by Cal-Am in its application.

Additionally, the staff resource requirements of this proceeding conflict with those of several other major proceedings, specifically, Investigation 07-01-022 (Conservation Rate Design), Rulemaking 06-12-016 (Revisions to the General Rate Case Plan), Cal-

¹ (See http://www.coastalconservancy.ca.gov/sccbb/0701bb/0701Board15a_San_Clemente_Removal_Proj.pdf and http://www.montereycountyweekly.com/issues/Issue.03-09-2006/cover/Article.cover_story)

Am’s Sacramento/Larkfield General Rate Case, and Golden State Water Region 1 General Rate Case. Due to current staff resource limitations, DRA requests additional time for submission of DRA testimony. DRA’s proposed schedule is below.

Extending the filing date for DRA and intervenor testimony in this proceeding will not financially harm or disadvantage Cal-Am in any respect because the Commission has authorized Cal-Am to “use the existing AFUDC at the 90-day commercial paper rate on the San Clemente Dam retrofit account, *subject to true-up*, until we complete our review of this issue in the upcoming application.”² Therefore, the schedule should be delayed until later this year, when adequate staff resources are available to devote to this application.

EVENT	DRA’S PROPOSED DATES
Application Filed	02/20/07
Protest Due	03/26/07
Replies to Protest	04/04/07
DRA/Intervenor Testimony	07/02/07
Utility Rebuttal Testimony	07/17/07
Evidentiary Hearings (if necessary)	07/30/07 to 07/31/07
Opening Briefs	08/13/07
Reply Briefs	08/20/07
ALJ’s Proposed Decision	10/20/07
Comments on Proposed Decision	11/09/07
Replies to Comments	11/15/07
Final Decision	11/26/07

² D.06-11-050, pp. 45-46 (A.05-02-012), (emphasis added).

V. CONCLUSION

For the reason stated above, DRA recommends that the Commission deny Cal-Am's request for an interest rate of 8.33% for AFUDC for its San Clemente Dam Memorandum Account and for authorization to place the estimated annual average cost of CWIP into rate base prior to the completion of the project. DRA will conduct discovery to develop its testimony and recommendations. Hearings may be required and a schedule should be established at the prehearing conference that allows for a thorough review of the application. Since DRA has not completed discovery or filed its report, it reserves the right to assert any issue discovered after this Protest has been filed.

Respectfully submitted,

/s/ Marcelo Poirier

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March 26, 2007

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of the foregoing document
**“PROTEST OF THE DIVISION OF RATEPAYER ADVOCATES TO THE
APPLICATION OF CALIFORNIA-AMERICAN WATER COMPANY”** in
proceeding A.07-02-023.

A copy was served as follows:

☒ **BY E-MAIL:** I sent a true copy via e-mail to all known parties of record
who have provided e-mail addresses.

☐ **BY MAIL:** I sent a true copy via first-class mail to all known parties of
record.

Executed in San Francisco, California, on the 26th day of March, 2007.

/s/ Nelly Sarmiento

Nelly Sarmiento

N O T I C E

Parties should notify the Process Office, Public Utilities
Commission, 505 Van Ness Avenue, Room 2000, San Francisco,
CA 94102, of any change of address and/or e-mail address to
insure that they continue to receive documents. You must indicate
the proceeding number on the service list on which your name
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